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SUBJECT: China Probes Intensified Taiwan Economic Engagement

BEIJING 00003782 001.2 OF 002

Classified By: Economic Minister-Counselor Robert Luke for
Reasons 1.4 (b) and (d)

11. (C) Summary. Contacts from the public and private sectors and several academics at government-affiliated think tanks expressed optimism over the direction of cross-strait economic engagement, attributing warming ties to the election of Ma Ying-jeou in March and Taiwan's efforts to manage an economic downturn. Contacts were most positive about the progress on transport links between China and Taiwan and expected upcoming meetings to work out remaining obstacles, such as establishing direct flights for both tourists and cargo. Progress on increasing the numbers of tourists who visit Taiwan would likely be slower, as the number of mainland travelers to Taiwan grows gradually over time as the program matures. Future rounds of cross-strait talks would likely turn to financial issues, such as investment guarantees and protections, improved currency clearing mechanisms, and opening Taiwan's stock markets to mainland capital. End Summary.

China Welcomes Economic Engagement with Taiwan

12. (C) Several embassy contacts pointed to Ma Ying-jeou's election and Taiwan's economic struggles as drivers of improving cross-strait economic engagement and characterized the mainland as happy to facilitate the expansion of economic links between the two. China Institute of Contemporary International Relations Research Fellow Yuan Chunqiang said the economic relationship between China and Taiwan has moved from one where the mainland provided most of the impetus to one that is more mutually cooperative. Chinese Academy of Social Sciences Institute of Taiwan Studies Fellow Sun Shengliang claimed Taiwan President Ma Ying-jeou was under a lot of pressure to improve the economy, prompting him to encourage visits from Chinese tourists, facilitate transportation links, and lift investment restrictions for Taiwan companies engaging in business in the mainland. Sun said China was trying to help Taiwan, but cautioned that China would move at a measured pace given its own concerns about Chinese citizens doing "illegal things," probably a reference to defections. Nonetheless, mainland Chinese businesses are increasingly positive about economic engagement with Taiwan, according to Yuan, as measures designed to showcase China's open and flexible economic policies towards Taiwan are no longer met with the hostility that characterized the Chen administration.

Expanding Transportation Links

13. (C) Contacts pointed to progress on the transportation issues as evidence of Taiwan's efforts to facilitate economic engagement with

the mainland and were positive on the potential for continued progress in the coming months.

Tsinghua University Institute of Taiwan Studies Professor

Liu Zhentao said direct flights between Taiwan and the mainland will begin next month, and he expected that direct cargo and postal flights would be discussed in late October ARATS-SEF talks, adding that the costs for Taiwan to delay the implementation of direct flights were too high. In Sun's view, Taiwan needed direct cargo flights and shipping because it depended on the quick return of electrical goods that are manufactured in the mainland. In addition to direct flights, contacts expected China and Taiwan to increase the number of departure cities for direct flights and permit more regular weekday flights. Sun said China and Taiwan could agree to flights nearly every day. The frequency would let Taiwan claim the flights were still "charters."

Tourism Fails to Meet Expectations

14. (C) China-Taiwan Travel Agency General Manager Feng Zhuozhi said procedures for prospective customers for the trips usually take at least two weeks and he criticized the mainland for being slower than Taiwan in approving permits for travel. So far, most mainlanders who had gone to Taiwan went to see relatives or scout business opportunities. Feng said his agency has separate departments to handle tourists who seek to establish business contacts and tourists primarily interested in sightseeing.

15. (SBU) Note: Starting July 18, 2008, mainlanders have been able to travel to Taiwan on tour-groups organized by State Tourism Administration (STA)-designated travel agencies. The number of travelers is subject to an STA-issued quota of 3,000 per day, in groups of 10-40 people, who can visit the island for up to 10 days. Prospective travelers first pay relevant travel fees to the agency, and then apply for permission to participate from the local Chinese public security office. Mainland travelers also post a "bond" of at

BEIJING 00003782 002.2 OF 002

least 50,000 RMB (about USD 7300) to ensure they return, and also must receive approval to visit from the Taiwan authorities. End Note.

16. (C) The number of mainland tourists traveling to Taiwan dropped off after the inauguration of weekend charter flights in July, but contacts characterized this as a temporary lull and expected the numbers to rise. According to the State Council Taiwan Affairs Information Office's Deputy Director General Huang Jianwen, the low number of tourists was due to the fact the program was new and involved complex procedures for arranging required permits. Other contacts agreed that these procedures are a main cause of the low number of tourists. Liu added that the high cost of roundtrip airfare also made a trip to Taiwan prohibitively expensive.

17. (C) Huang added that the program was being implemented slowly. Currently, only residents of the 13 "most developed" provinces were allowed to participate. Feng said Taiwan's strategy of seeking high-end tourists contributed to the low number, especially because a majority of China's high income earners, including government and some state-owned enterprise (SOE) officials, were not yet permitted to go to Taiwan. Feng claimed he was lobbying officials in the State Council's Taiwan Affairs Office to have these restrictions lifted.

Financial Issues on the Horizon

18. (C) One goal of upcoming discussions would be to normalize economic relations, particularly in areas related to investment and banking. Looking ahead to 2009, Sun expected both sides would use future talks to discuss MOUs aimed at providing stronger investment guarantees, improving currency clearing mechanisms, and opening Taiwan's stock markets to mainland capital. Sun and Yuan predicted that Taiwan would relax current prohibitions on mainland investment and Yuan said some SOEs would probably look to invest in Taiwan, particularly in the island's real estate and tourism sectors. The mainland, meanwhile, is considering loosening regulations that

restrict Taiwan-based banks' ability to establish mainland operations, and is reportedly considering permitting Taiwan banks to establish branch offices to be used by Taiwan businessmen.

Comment - Economic Ties Could Help Resolve Political Issues

19. (C) A subtext of the meetings was that Taiwan has become increasingly dependent on the mainland economy, and that by helping Taiwan economically, the mainland was building capital that it could leverage to address more complicated issues, such as Taiwan's diplomatic status. Several contacts clearly saw closer economic links as a first step to future cooperation on "thornier" political and security challenges, and expressed confidence that successful resolution of the economic issues would make tackling the other issues easier, though they were reluctant to speculate on the details.

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